

STATE OF TENNESSEE

Office of the Attorney General



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April 8, 2002

Mr. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: United Cities Gas Petition for Approval
of New or Revised Franchise, Agreement
with Kingspot, Bristol, Morristown and
Maury County
Docket No. 00-00562

Dear Mr. Waddell:

Enclosed is an original and thirteen copies of the Post Hearing Brief of the Attorney General in the above-referenced matter. Copies are being furnished to counsel of record for interested parties.

Sincerely,

Timothy C. Phillips

TIMOTHY C. PHILLIPS
Assistant Attorney General

cc: Counsel of Record
54121

POSTED
4/8/02

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE:

UNITED CITIES GAS PETITION FOR)	
APPROVAL OF NEW OR REVISED)	
FRANCHISE AGREEMENTS WITH)	Docket No. 00-00562
KINGSPORT, BRISTOL, MORRISTOWN)	
AND MAURY COUNTY)	
)	
)	
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POST HEARING BRIEF OF THE ATTORNEY GENERAL

The Tennessee Attorney General, through the Consumer Advocate and Protection Division ("Attorney General"), files this post hearing brief. To assist the Hearing Officer, this brief is submitted in the form of proposed findings of fact and conclusions of law.

By statute, this Tennessee Regulatory Authority (hereinafter, "Authority") is charged with the obligation of reviewing the franchise agreements before it in the United Cities Gas Petition. Pursuant to Tenn. Code Ann. § 65-4-107, the Authority must determine whether or not the franchise agreements before it are "necessary and proper for the public convenience and properly conserves the public interest" and whether or not to modify the franchise agreement as appropriate. The Authority's analysis begins with its review of the current law.¹ Second, this

¹ The Hearing Officer has asked that the briefing submitted by the parties regarding the summary judgment on behalf of United Cities Gas not be reviewed in the post hearing briefing. The Attorney General is comfortable with the briefing on the issues confronted in the summary judgment motion and will of course honor the Hearing Officer's request. It is important to note however that much of the discussion concerning the summary judgment motion is important to the Authority's review of the of the subject franchise agreements as to legality and whether or not

Authority, after its review of the current law, may find it lacking or outdated and determine that modifications to the current law are appropriate. Third, the Authority considers the impact of the subject franchise agreements on the "public convenience" and the "public interest" in light of current law and the policy of this Authority.

FINDINGS OF FACT

At the very beginning of the "negotiations" of the franchise agreement between United Cities Gas and the Cities of Morristown and Bristol, the first step by the city was to threaten United Cities Gas with its powers of eminent domain.²

The franchise fee is not listed or otherwise disclosed in the bills or invoices sent to the residents of the City of Morristown. Tr. 50.

The City of Morristown collected approximately \$500,000.00 in franchise fees in the year 2001. Tr. 50-51.

The customers of United Cities Gas in the City of Morristown pay for all expenses incurred by United Cities Gas. Tr. 51-55. Its revenues come from the customers in the city. Tr. 51-55. Through these revenues United Cities Gas pays its expenses, such as storage costs, distribution costs, taxes, payroll, the cost of billing, debt service and profits. Tr. 51-55.

The witness United Cities Gas offered at the hearing was not the individual primarily responsible for the "negotiations" between United Cities Gas and the City of Morristown. Tr. 57. However, as far as his participation, he at no time questioned the validity of the franchise fee the

the franchise agreements are indeed necessary to the "public convenience" and "properly conserves the public interest."

²Tr. 45, 115-116; Direct testimony of John Collins, Mayor John R. Johnson, Jim Pugh and City Manager Anthony R. Massey.

city of Morristown demanded United Cities Gas pay. Tr. 57.

United Cities Gas does not have any competitors in the area of the city of Morristown. Tr. 58-59.

United Cities Gas is not aware of the market value of the rights of way it is leasing through the franchise agreement from the City of Morristown. Tr. 59.

United Cities Gas' witness testified that 5% was the highest fee he was aware of being charged as a franchise fee for the supply of gas. Tr. 59. He was aware that there are municipalities who do not charge a franchise fee. Tr. 60.

There can be little question as to the weight of the city's threat of using the power of eminent domain. Tr. 63-64. United Cities admits that the cities' threat was of the degree that United Cities acted contrary to its will and inclination. Tr. 63-64. United Cities Gas was simply in a position of agreeing to whatever the city wanted because it feared losing its system. Tr. 63-64. United Cities Gas' witness knew of no instance during the "negotiations" in which United Cities Gas objected to paying the 5% franchise fee to the City of Morristown. Tr. 65. The witness presented by United Cities Gas was unsure as to what the upper limit should be for a franchise fee and unsure if a fee as high as 10% would be appropriate. Tr. 67.

The witness from the City of Morristown verified that the city had threatened United Cities Gas with seizure of its properties. Tr. 81. The officials representing the city in the "negotiations" took the payment of the franchise fee as a given. Tr. 84. There were no "negotiations" with respect to the amount of the franchise fee. Tr. 85.

The city of Kingsport does not seek approval of a franchise fee. Tr. 16. The City of Kingsport at no time threatened United Cities Gas with seizure of its properties. Tr. 14, 20, 25,

and 26. The officials representing Maury County, in their "negotiations" with United Cities Gas, did not threaten to seize it's property through eminent domain. Tr. 34. There is no request for a franchise fee in the Maury County franchise agreement.

The franchise fee is used by the City of Morristown for general purposes. The City of Morristown actually earmarks the fee for the development of its industrial park. Tr. 85. The witness for the City of Morristown admitted the franchise fee takes the place of property taxes. Tr. 85. The City of Morristown uses the franchise fee to "keep their property taxes low." Tr. 85. In fact, the City of Morristown has not raised its property tax in seventeen (17) years. Tr. 86. The City of Morristown noted that this was the direct result of its extraction of a franchise fee. Tr. 86-87.

The City of Bristol presented to the Authority many documents related to the "negotiations" between the Bristol and United Cities Gas. Exhibit 4, Tr. 138. Out of 35 documents totaling just over 200 pages, there are six (6) general references to the subject of a franchise fee. Only one (1) document expresses a negative reaction to an increase (see Item #19 Letter of Dec.11, 1997) that is proposed to settle differences between the city and United Cities Gas (see Item #18 "Points of discussion" memo dated 8/ 19/97).

Most of the documents that feature some form of debate or "negotiation" revolve around the subject of property leases and liability issues of the use of those properties.

Below is a list of all documents with any reference to the subject of a franchise fee.

Item #4:(9/23/95) Fax from Gary W. Price (U.C.G.) to Sandra Schofer in which there is a draft of Section XIII of the agreement which lays out the franchise fee.

Item #7:(10/3/95) Minutes of City Council meeting of October 3, 1995; Schofer gave brief description of franchise agreement and no comments were made.

Public hearing was then closed.

Item #18:(8/19/97) A city memo titled "Points of Discussion with U.C.G." in which item C states a desire to discuss a franchise fee increase.

Item #19: (12/11/97) Letter from U.C.G. president Thomas Blose to city manager Tony Massey regarding a proposal to settle dispute over merger. A franchise increase to 6% is agreeable to both parties, but UCG voices concerns over the price of gas becoming uncompetitive with other providers.

Item #29: (6/1/99) Minutes of City Council meeting of June 1, 1999. Under the "New Business" section, item B describes Ordinance 99-13 which amends the franchise agreement for an increase of the franchise "tax" from five to six percent (5%-6%).

Item #32: (8/5/99) Minutes of City Council meeting of August 5, 1999. Under section titled Public Hearing/Old Business in item A, Ordinance 99-13 amending the Franchise Agreement with a fee increase to 6% is passed after a public hearing. No comments were made by the public in attendance.

The budget for the City of Morristown is twenty million (\$20,000,000,000) dollars. Tr.

87. Within the city limits there are approximately 25,000 residents. Tr. 88.

The City of Morristown does not impose a franchise fee on any other energy suppliers.

Tr. 89. The City of Morristown supplies electricity to its citizens. Tr. 89.

These franchise fees are collected by United Cities Gas from its customers and then paid to the city as a franchise fee. Tr. 90.

Every dollar the city collects from the franchise fee goes to pay for an industrial park in the City of Morristown. Tr. 93.

The franchise fee agreement and the ordinance approving it was not voted on by the citizens of the City of Morristown. Tr. 95.

The city of Morristown did not do any studies with respect to the costs associated with maintaining the rights of way that United Cities Gas would use. Tr. 96. The City of Morristown

did not make any analysis or study with respect to the value of the rights of ways. Tr. 96. The rights of ways are used for vehicular traffic. Tr. 97. The city believes that these rights of ways do have value as conduits of business, trade, commerce and commuting. Tr. 97

When asked, the witness for the City of Morristown was unable to provide any real answer to the question of how it is in the public interest to raise money through franchise fees in the place of property taxes. Tr. 99. The following question and answer reveals that the city and United Cities Gas have not the slightest notion of why or how a franchise fee should be limited.

- Q. Let me ask you another question. What reason would the city or the Gas company in this case have for eliminating [or] limiting the franchise fee?
- A. What reason? *Well, I guess I could only speculate.* You would want to have, you wouldn't want 100% franchise fee; you wouldn't have any gas company. Its like an economic decision. If it's a common method of collecting income, can you so it so its fair to the folks involved and reasonably affective to provide the service you're after? Tr. 100. (emphasis added)

The City of Morristown believes a 5% franchise fee is appropriate solely because other cities were doing the same thing. Tr. 102-103.

The citizens of Bristol who are customers of United Cities Gas provide its revenue. Tr. 122-124. In other words, the customers pay for the gas supplied to them. Tr. 122. The customers pay for United Cities Gas' storage costs, sales tax, property taxes, payroll, debt service and of course, a profit or margin between their gross receipts and expenses. Tr. 123-124.

United Cities Gas has approximately 4,500 customers in the City of Bristol. This makes up a small portion of the individuals benefitting from the franchise fee. United Cities Gas serves

approximately 4,750 customers in the City of Morristown.³ The United Cities Gas customers make up a small portion of the individuals benefitting from the franchise fee.

United Cities Gas never made a counter offer to the 6% franchise fee demanded by the city of Bristol. Tr. 127. United Cities Gas did not make any analysis of the city's costs of maintaining its rights of way costs. Tr. 129. Nor did United Cities Gas make any analysis of the market value of the rights of way. Tr. 129. The 6% franchise fee charged by the City of Bristol is the highest in Tennessee. Tr. 131.

As part of its remuneration to the city in exchange for the grant of the franchise fee, United Cities Gas has actually allowed the city free parking. Tr. 144.

The city manager for the City of Bristol who "negotiated" with United Cities Gas had significant experience running a natural gas system for a city. Tr. 146. United Cities Gas was aware of the background of the city manager of Bristol, Tennessee during the "negotiations" over the franchise agreement. Tr. 159-160. In the winter of 1997, the city manager and the mayor of the City of Bristol discussed the possibility of the city of Bristol taking over the gas supply business from United Cities Gas with individuals from the Tennessee Regulatory Authority. Tr. 147. The individuals at the Tennessee Regulatory Authority advised him that it would not be a good idea. Tr. 147. There are other reasons outlined in a testimony which make it unlikely that the city of Bristol would ever actually take over the gas supply system from United Cities Gas. Tr. 146.

The officials from the City of Bristol were acting in a dual capacity during the "negotiations" with United Cities Gas. Tr. 151. In fact, the city officials of the City of Bristol

³Exhibit A to Direct Testimony of John Collins.

felt a fiduciary obligation towards its citizens in its negotiation with United Cities Gas over the franchise agreement. Tr. 151. The officials of the City of Bristol claim that they sought to do what they thought was fair to the citizens of Bristol and United Cities Gas. Tr. 151.

The officials of the city of Bristol did little to notify the citizens of Bristol or educate them as to what is in their gas bill with respect to the franchise fee. Tr. 153.

The population of the City of Bristol is approximately 25,000 people. Tr. 154. The budget for the City of Bristol for the current year is over twenty million (\$20,000,000,000.00) dollars. Tr. 154. The City of Bristol collects on the average \$300,000.00 a year in franchise fees from the customers of United Cities Gas. Tr. 154. Most of the customers in the City of Bristol have heat in their homes. Tr. 155.

The only other franchise fee charged by the city of Bristol is to the cable company. Tr. 155.

The parking lot that United Cities Gas allows Bristol to use for free is not only used by the citizens of Bristol but also the citizens of Sullivan County. Tr. 155-156. The subject parking lot is used by individuals who do not pay the franchise fee. Tr. 156. There are approximately 150,000 people in the County of Sullivan. Tr. 156. The ordinance approving the franchise agreement between United Cities Gas and the City of Bristol was approved by the Bristol city council. Tr. 156. It was not put to a vote by the public or the citizens of Bristol, Tennessee. Tr. 157.

The money generated from the franchise fee goes into the general fund for the general purpose and use by the City of Bristol. Tr. 157.

The City of Bristol has not performed any cost studies with respect to the cost attributable

to United Cities Gas use of its rights of ways for supplying gas to the citizens of Bristol, Tennessee. Tr. 157-158. The city of Bristol did not do any analysis of the market value of the rights of ways used by United Cities Gas. Tr. 158.

Monies from United Cities Gas to the city of Bristol have been used for work in the public library. Tr. 158. Additionally, monies have been used for the restoration of a country music mural in downtown Bristol. Tr. 158-159. The franchise fee collected by the city of Bristol goes to the general fund and is used for any needs that the city may have. Tr. 159.

United Cities Gas never made a counter offer of any sort to the 6% franchise fee demanded by the city of Bristol. Tr. 161. The city manager for the City of Bristol recognizes that there is a reasonable limit to the amount that the City of Bristol could charge in a franchise fee. Tr. 162.

The highest franchise fee charge in the State of Tennessee is 6%. Tr. 163. The lowest is zero. Tr. 163.

As is in the case of the City of Morristown and the City of Bristol, the collection of the franchise fee helps the city in not having to raise its property tax. Tr. 164.

The city manager for the City of Bristol cited fairness as the only limitation the city placed on the percentage it charged for the franchise fee. Tr. 164.

There is no evidence in the record suggesting that the franchise fee is cost based. There is no evidence in the record suggesting that the franchise fee is based on the market value of the rights of way owned by the City of Bristol or the City of Morristown. Without some cost information as a basis for the franchise fee, it is essentially arbitrary from an economic standpoint. Tr. 175.

The City of Bristol, the City of Morristown and United Cities Gas petition proceeds without any type of any rational economic approach. Tr. 175. There is no apparent connection between the economic activity surrounding the performance of the service and the actual franchise fee that is collected. Tr. 173.

CONCLUSIONS OF LAW

In the *Order Denying Motion For Partial Summary Judgment Without Prejudice*, date February 15, 2002, the Hearing Officer charged United Cities Gas, and the cities of Bristol and Morristown, with the obligation to prove that the franchise fee was the product of real negotiations and consent. United Cities Gas and the Cities of Bristol and Morristown have failed to do so. Instead, it is obvious from the evidence in this record that the franchise fee was simply imposed upon United Cities Gas by the Cities of Bristol and Morristown.

Further, the hearing in this matter produced no additional evidence repudiating the conclusion that the franchise agreements between United Cities Gas and the Cities of Bristol and Morristown clearly impose new requirements on United Cities Gas and altered or revoked pre-existing franchise rights.⁴

The testimony in this matter, indicates that the economic stress that United Cities Gas was working under negates any semblance of real negotiation between the parties of the franchise agreements. United Cities had little choice in this instant but to capitulate to the demands of the Cities of Bristol and Morristown. "Economic duress" is defined as "so coercive and severe that a person or ordinary firmness could not resist it." *Dockery v. Massey*, 958 S.W.2d 346, 348 (Tenn.

⁴ The briefs, and the attachments thereto, of the parties regarding the summary judgment motion describe the alterations to the franchise agreements involved.

App. 1997). There was little United Cities Gas could do in this instance. United Cities Gas has offered little in the way of proof demonstrating that it had any reason to resist the imposition of franchise fees on its customers. United Cities Gas' allegiance is to its stockholders. Getting the franchise agreements executed and approved are its primary goal. United Cities is allowed to pass along the fee to consumers. It loses nothing in the exchange. Especially, considering that these fees are passed on without itemization on the consumer's bill.

The entire circumstances are, of course, complicated by the fact that the city serves two masters: itself (and the general population) and the customers of United Cities Gas who live inside its city limits. The city owes a fiduciary obligation of trust to the customers of United Cities Gas. *Fleming vs. City of Memphis* 126 Tenn. 331, 148S.W.1057(1912); *McKay vs. Dupont Rayon Company*, 20 Tenn. App.157, 96 S.W.2d 177(1935); *Board of Directors of St. Francis Levee District vs. Bodkin* 108 Tenn. 700, 69 S.W. 270(1902).

Both the cities and United Cities Gas intimate that they somehow represent the consumers involved. In fact, the cities and United Cities Gas get precisely what each wants at the expense of the customers.

As such, United Cities Gas and the Cities of Bristol and Morristown can not rely on the suggestion that this was an arms-length deal. Therefore, the franchise fee requested must be supported by some type of market analysis reflecting that the rents for the rights of way are reasonable.

In actuality, neither party was concerned about the customers of United Cities Gas. The goals of United Cities Gas and the Cities of Bristol and Morristown move in lock step. Nor were the customers of United Cities Gas represented in the "negotiations". These parties did not deal at arms-

length. *Detriot Auto Dealers Association, Inc. v. FTC*, 955 F2d. 457, 463-464 (6th Cir. 1992).

The record is clear and strong: the franchise agreements are not the result of arms-length negotiation between the cities and United Cities Gas. Instead, the record recounts United Cities Gas' willing acquiescence to municipal authority because the franchise fee comes not from the company, but from consumers who ultimately pay those fees. The record further proves the cities are unwilling to temper their franchise authority with any economic method aimed at developing a just price for a utility's private use of public resources.

The Authority's statutory duty to decide this case would have little significance if the central issue were simply to reaffirm the cities' authority. The central issue is whether the cities' authority is to be tempered by a judicial assessment of the fees' "reasonableness." The Authority's ultimate decision should give substantial weight to "reasonableness," which should be a primary consideration in the final decision.

REMEDIES

Although United Cities Gas and the Cities of Bristol and Morristown cite the *City of Chattanooga vs. BellSouth Telecommunications* case as allowing it to charge a franchise fee in excess of the costs for maintaining the rights of way, it is clearly an expansion on Tennessee case law to suggest that the franchise fee need not relate to the rental values of the rights of way. In other words, without some type of reasonable value placed on the rights of way, the franchise fee is essentially arbitrary and inconsistent with current Tennessee law and reasonable public policy. The correct approach is to require some type of support for the fee. The rates must be reasonable. Tenn. Code Ann. § 65-5-201.

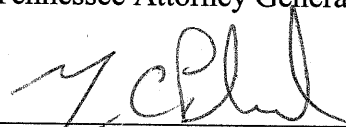
If neither United Cities Gas nor the cities involved are able to substantiate the subject

franchise fee as reasonable then the petition should be denied or altered by removing the fee all together.

Alternatively, the Authority might set the rates at an amount between that accessed in the case of Maury County and that sought by the City of Bristol. Taking the subject franchise agreements as a whole, the franchise fees requested range from 0% of gross revenues to 6% of gross revenues. There is nothing in the evidence to support the proposition that the agreements are in the public interest. In fact, the only factual distinctions between the two agreements which call for a franchise fee and the two agreements which do not seek approval of a franchise fee are the improper negotiating posture taken by the City of Morristown and the City of Bristol. More specifically, there is no evidence in the record suggesting a valid and reasonable justification for the city of Bristol needing a 6% franchise fee as specified under the present franchise agreement as opposed to the two and one half percent (2 ½ %) it sought approval for in 1983. A rate of 2 ½ % is as just and as reasonable as that proposed by United Cities Gas and the Cities of Morristown and Bristol.

Respectfully submitted,

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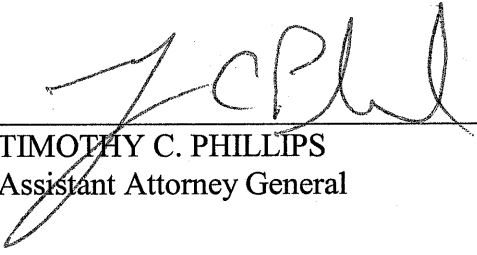
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